

Market Recap

Select Years S&P 500 Returns



Source: Bloomberg

S&P 500 Performance and Earnings Forecasts



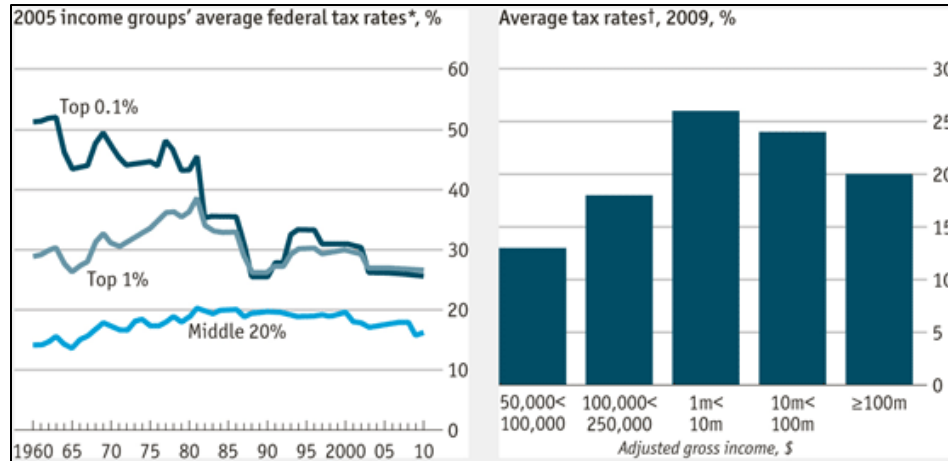
Source: WSJ; S&P Capital 1Q (earnings)

Investors have been drawing comparisons between the start of this year and the two previous years. In both 2010 and 2011, an early run-up in the stock market, similar to this year, pushed stocks up about 10% by mid-April; the market then went on to fall 16% and 19% respectively from those levels. Many investors attribute the similar market movements to the economic stimulus measures of the Federal Reserve. In each of the past two years, fiscal stimulus programs known as QE1 and QE2 came to an end in the spring or summer. Stocks began their decline until the next program was announced. The current program, known as 'Operation Twist,' is scheduled to conclude at the end of June. The thinking of some investors is that the stock market may continue to experience weakness until another program such as QE3, which was recently hinted at by the Fed, is announced. What remains to be seen is how the market reacts to the current decline for the balance of the year. In 2010, the market was able to recoup its spring sell-off to finish the year with a 15% gain. Last year, the market never regained its spring peak and finished the year largely unchanged.

This week marked the start of the corporate earnings season. Many analysts are forecasting lackluster results. Despite the stock market rise, analysts have been ratcheting down their expectations for company earnings throughout the first quarter. This raises the prospect that investors may be in for a surprise when companies announce their first-quarter results. Analysts have lowered expectations for both first-quarter and full-year earnings. They now expect earnings to show average growth of just 0.95% over a year earlier in the first quarter. That would be the lowest rate of year-to-year growth since the end of the financial crisis, and down from expectations of 4.5% growth in early January. By comparison, S&P 500 earnings rose 8.4% in the fourth quarter and 18% in the third quarter of 2011.

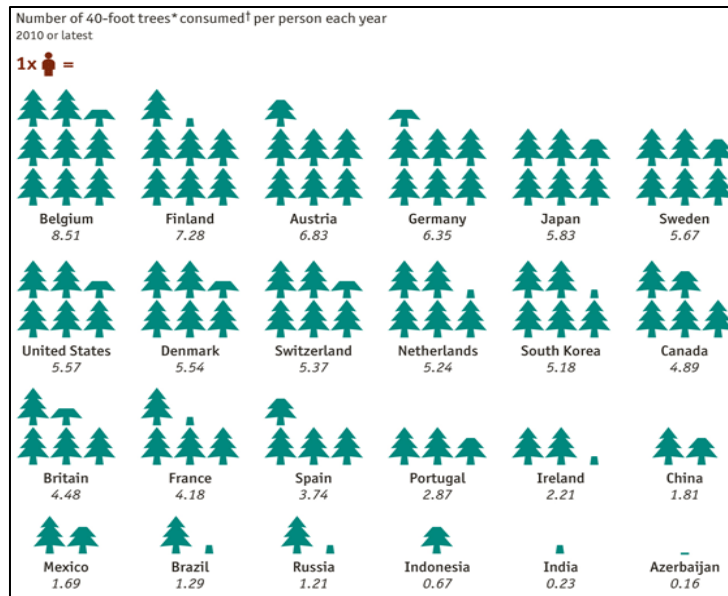
Market Recap

U.S. Tax Policy



Source: National Economic Council

Paper Consumption



Source: RISI; Bureau of International Recycling

The Obama administration has been pushing for a change in tax policy that it calls the 'Buffett Rule' after investor Warren Buffett. Their view is that the current tax code is unfair, as Mr. Buffett pays a lower average tax rate than his secretary pays. According to the President's National Economic Council, the average tax rate paid by households with income between \$1m and \$10m in 2009 was just over 25%. Average rates actually decline from those levels for higher incomes. Households earning more than \$100m paid 20% in tax on average. The very affluent typically pay lower rates because much of their income is qualified dividend and capital gain income (taxed at lower rates). The Buffett Rule stipulates that households earning over \$1m a year would face a minimum total tax rate of 30%. Critics of the proposal counter that the median effective tax rate for the middle 20 percent of U.S. taxpayers is 13.3 percent and for the top 1 percent is 29.6 percent. The top 1% of earners pay more than a quarter of total Federal taxes and about 40% of Federal income taxes. The top 10% of earners pay 70% of Federal income taxes and the top 50% pay 98%.

With the advent of the computer era, we were supposed to be headed to the 'paperless office.' Since 1980, global paper consumption has increased by 50%. The average American uses the paper equivalent of almost six 40-foot trees per year. Belgium is the biggest consumer of paper with almost 9 trees per person. Paper consumption is pushed up by the bureaucracy of the European Union in Brussels, which must produce its documents in an array of different languages. Paper consumption (production plus imports minus exports) can be distorted, as it includes paper exported as other products. Nonetheless, the demand for paper has actually increased since the advent of the computer era and does not seem to be waning as computer adoption grows and extends to more nations.

Contact: If you have any questions or comments, please do not hesitate to contact us at 703.992.6164. For more information about Harbour Capital Advisors, please visit our website at www.harbourcapitaladvisors.com.

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